

Message Text

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PAGE 01 OECD P 14128 01 OF 02 130008Z
ACTION EUR-12

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LIMITED OFFICIAL USE SECTION 01 OF 02 OECD PARIS 14128

PASS: CEA, TREAS, FRB

E.O. 11652: N/A
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SUBJECT: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE
(EDRC) REVIEW OF GREECE

REF: (A) EDR(77)11; (B) STATE 103031

1. SUMMARY: DESCRIPTION OF GREEK ECONOMIC PERFORMANCE
IN 1976 BY GREEK DEL (LED BY LEMONIAS, DIRECTOR GENERAL,
MINISTRY OF COORDINATION) LED SOME COUNTRY REPS AND
SECRETARIAT TO DESCRIBE GREECE AS "GERMANY OF SOUTHERN
EUROPE." MOREOVER, NEITHER GREEKS NOR SECRETARIAT
FORESEE MARKED REVERSAL IN 1977 OF FAVORABLE DEVELOPMENTS
DURING 1976. HOWEVER, SECRETARIAT WAS SKEPTICAL THAT
GREEKS WOULD BE ABLE TO ACHIEVE OFFICIALLY TARGETED
INFLATION RATE (10 PERCENT) IN 1977; GREEKS CONSIDERED
THIS TARGET FEASIBLE. GREEKS SUPPORTED SECRETARIAT (AND
EDRC) VIEW THAT INCREASED INVESTMENT WAS KEY TO EFFECT-
ING STRUCTURAL CHANGES IN GREEK ECONOMY OVER MEDIUM TERM,
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PAGE 02 OECD P 14128 01 OF 02 130008Z

BUT TOOK ISSUE WITH VIEW EXPRESSED BY SOME DELS THAT
RECENT CHANGES IN TAX SYSTEM (E.G., TAX ON DIVIDENDS)
MILITATED AGAINST ACHIEVING THIS OBJECTIVE. IN THIS CON-
TEXT, GREEKS RESISTED SECRETARIAT CONTENTION THAT DELAY
IN FORMULATING AND ANNOUNCING INVESTMENT INCENTIVE PRO-
VISION OF NEW FIVE-YEAR PLAN (1976-80) HAD ADVERSE EFFECT
ON INVESTMENT SPENDING, NOTING THAT CERTAIN ELEMENTS OF

PLAN HAD BEEN IN FORCE SINCE 1976. EDRC CONCLUDED BY URGING GREEKS TO INTENSIFY EFFORTS TO GET INFLATION DOWN AND TO STIMULATE INVESTMENT AND BY EMPHASIZING IMPORTANCE OF STRUCTURAL CHANGE IN GENERAL AS WELL AS IN RELATION TO POSSIBLE ENTRY OF GREECE INTO COMMON MARKET. END SUMMARY

2. SHORT-TERM PROSPECTS; DOMESTIC OUTLOOK FOR 1977: IN 1976, GREEKS CONTINUED REAL GDP (AT FACTOR COST) GROWTH OF 5.4 PERCENT AND FALL IN UNEMPLOYMENT RATE WITH DECLARATION OF INFLATION--A PERFORMANCE WHICH INDUCED SOME DELS AND SECRETARIAT TO CHARACTERIZE GREECE AS "FRG OF SOUTHERN EUROPE". GREEKS FORECAST MORE OF THE SAME IN 1977: GROWTH REAL GDP AT FACTOR COST OF 5-5.4 PERCENT (6-7 PERCENT GROWTH OF REAL GNP AT MARKET PRICES); 2.1 PERCENT INCREASE IN EMPLOYMENT AND 10 PERCENT RISE IN CONSUMER PRICES. SECRETARIAT WAS LESS SANGUINE THAN GREEKS CONCERNING INFLATION OUTLOOK, NOTED THAT UNDERLYING INFLATION RATE WAS HIGH AND THAT RECENT SHARP INCREASES IN COMMODITY PRICES POSED ADDITIONAL INFLATIONARY RISK. GREEK ARGUMENT THAT PRICE CONTROL SYSTEM WOULD BE ADEQUATE TO PERMIT ACHIEVEMENT OF 10 PERCENT INFLATION (CPI) TARGET CONVINCED NEITHER SECRETARIAT NOR EDRC.

3. SOME COUNTRY DELS SKEPTICAL THAT 7-8 PERCENT RISE IN GROSS FIXED INVESTMENT IN 1977 FORECAST BY GREEKS WOULD MATERIALIZE AND COMMENTED THAT (A) STRONG RISE UNIT LABOR COSTS IN 1976 LIKELY TO HAVE PRODUCED PROFIT SQUEEZE; AND (B) IMPLEMENTATION OF TAX ON DIVIDENDS LIMITED OFFICIAL USE

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PAGE 03 OECD P 14128 01 OF 02 130008Z

WOULD ADVERSELY EFFECT FINANCIAL POSITION OF FIRMS AND BUSINESS CONFIDENCE. GREEKS POINTED OUT THAT (A) RISE IN SHARE OF WAGES IN NATIONAL INCOME HAD BEEN POLICY OBJECTIVE OF GOG OVER LAST TWO YEARS, SINCE THIS RATIO HAD FALLEN BELOW ITS LONG-TERM LEVEL PRIOR TO 1973 (WAGE BILL AS PERCENT OF NATIONAL INCOME ROSE FROM 44.2 PERCENT TO 48.2 PERCENT BETWEEN 1973 AND 1976); (B) BUSINESS PROFITS ADEQUATE. HOWEVER, IT WOULD BE DESIRABLE IF PROFITS AS PERCENT OF BUSINESS TURNOVER WERE TO FALL FROM 12 PERCENT REGISTERED IN 1976 TO 6-7 PERCENT; (C) INVESTMENT HAS HELD UP REASONABLY WELL IN SMALL TO MEDIUM-SIZED FIRMS; APPARENT WEAKNESS STEMS FROM POSTPONEMENT OF A FEW LARGE-SCALE PROJECTS; (D) MAIN FACTOR INFLUENCING INVESTMENT NEXT YEAR WILL BE STATE OF OECD AREA ECONOMY RATHER THAN RECENT CHANGES IN TAX PROVISIONS.

4. SECRETARIAT SUGGESTED THAT DELAY IN PROMULGATING INVESTMENT PROVISION OF NEW FIVE-YEAR PLAN HAS PROBABLY

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PAGE 01 OECD P 14128 02 OF 02 130012Z
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LIMITED OFFICIAL USE SECTION 02 OF 02 OECD PARIS 14128

DETERRED INVESTMENT. GREEKS DOUBTED THAT THIS WAS THE CASE AND NOTED THAT CERTAIN POLICIES (UNSPECIFIED) CONTAINED IN THE PLAN HAD BEEN APPLIED DURING 1976. GREEKS ADDED THAT NEW INVESTMENT INCENTIVES WOULD HAVE TO BE TAILORED TO EC PRACTICES AND INDICATED THAT ASSURING SUCH CONFORMITY HAD BEEN MAIN REASON FOR DELAY IN FINALIZING THIS PORTION OF PLAN. GREEKS ALSO SAID, HOWEVER, THAT IT MIGHT BE NECESSARY FOR FIRMS TO OPERATE UNDER AN INTERIM INVESTMENT REGIME DURING TRANSITION PHASE PRIOR TO FULL EC MEMBERSHIP. EDRC CONCLUDED THAT UNCERTAINTY AS REGARDS INVESTMENT POLICY LIKELY TO INDUCE "WAIT AND SEE" ATTITUDE ON PART OF BUSINESS.

5. CURRENT ACCOUNT PROSPECTS FOR 1977: DETERIORATION OF TRADE BALANCE IN 1976 WAS OFFSET BY RISE IN INVISIBLES SURPLUS, WITH RESULT THAT CURRENT ACCOUNT DEFICIT STABILIZED AT 1975 LEVEL OF ABOUT \$1 BILLION. DEFICIT LARGELY FINANCED BY AUTONOMOUS PRIVATE CAPITAL INFLOWS (PRIMARILY DEPOSITS BY GREEKS LIVING ABROAD) MOST OF

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PAGE 02 OECD P 14128 02 OF 02 130012Z

WHICH WERE SUBSEQUENTLY SPENT IN DOMESTIC ECONOMY. GREEKS EXPECT CURRENT ACCOUNT DEFICIT FORECAST FOR 1977 (\$1.2 BILLION) TO BE FINANCED IN SIMILAR MANNER. U.S. DEL CRITICIZED SECRETARIAT RECOMMENDATION IN REFDOC THAT GREEKS PLACE INCREASING RELIANCE ON SUPPLIERS CREDITS AS OPPOSED TO FORM OF FINANCING OUTLINED ABOVE. GREEKS AGREED AND POINTED OUT THAT AMOUNT OF OUTSTANDING SUPPLIERS CREDITS (\$1.2 BILLION IN 1976, CONSTANT AT 1975 LEVEL DUE TO OFFSETTING CHANGES IN BORROWING AND REPAYMENTS) SHOULD NOT BE PUSHED MUCH HIGHER. SECRETARIAT FUSSED A BIT, BUT AGREED TO DELETE RECOMMENDATION FROM REVISED DRAFT SURVEY, WHILE RETAINING SUGGESTION THAT GREEKS DEVELOP FORWARD EXCHANGE MARKET TO FACILITATE ACCESS TO CAPITAL MARKETS IN FUTURE.

6. IN RESPONSE TO U.S. QUESTION PER REF B, GREEKS INDICATED THAT TOTAL OUTSTANDING FOREIGN DEBT AT END OF 1976 WAS \$3.76 BILLION (CONVERTED AT DECEMBER, 1976 EXCHANGE RATE). OF THIS, PUBLIC DEBT WAS \$2.14 BILLION (CATEGORY INCLUDES LIABILITIES OF CENTRAL GOVERNMENT, BANK OF GREECE, PUBLIC ENTERPRISES AND PUBLICALLY GUARANTEED DEBT). TOTAL OUTSTANDING FOREIGN DEBT WAS \$3.56 BILLION AT END OF 1975, WITH \$200 MILLION RISE DURING 1976 ATTRIBUTABLE TO INCREASE IN PRIVATE BORROWING. DEBT SERVICE RATIO (INTEREST AND AMORTIZATION PAYMENTS AS PERCENT OF EXPORT RECEIPTS) STOOD AT 10 PERCENT AT END OF 1976.

7. EFFECTIVE (TRADE WEIGHTED) DRACHMA EXCHANGE RATE DEPRECIATED BY 7 PERCENT DURING 1976. GREEKS CONSIDERED THIS MOVEMENT APPROPRIATE IN LIGHT OF RELATIVE COST DEVELOPMENTS AND INTEND TO LET EXCHANGE RATE MOVE IN RESPONSE TO RELATIVE COST MOVEMENTS IN 1977. (U.S. RESISTED TEMPTATION TO APPLAUD THIS STATEMENT.)

8. FISCAL AND MONETARY POLICY: GREEKS NOTED THAT BOTH FISCAL AND MONETARY POLICY WOULD BE MORE RESTRICTIVE IN LIMITED OFFICIAL USE

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PAGE 03 OECD P 14128 02 OF 02 130012Z

1977 THAN LAST YEAR. EDRC DISCUSSION OF GOG DEMAND MANAGEMENT POLICIES WAS MINIMAL. GREEKS EMPHASIZED MEASURES THEY HAD TAKEN TO REDUCE TAX AVOIDANCE AND EVASION AND, IN RESPONSE TO QUERY BY EC REP, STATED INTENTION OF ADOPTING VAT.

9. GREEKS SUPPORTED EDRC CONCLUSIONS THAT LONGER-RUN HEALTH OF GREEK ECONOMY DEPENDED ON ACHIEVEMENT OF EFFECTIVE CONTROL OVER GROWTH OF WAGES AND PRICES AND

ON GENERATING INCREASE IN INVESTMENT NECESSARY TO ADAPT
STRUCTURE OF GREEK ECONOMY TO CHANGING WORLD ENVIRON-
MENT.

10. QUESTION RAISED PARAS 1 AND 2, REF B ADDRESSED
PARAS 2 AND 6.
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